April 20, 2012

Mr. George Pullen
Commodity Futures Trading Commission
Washington, D.C.

By email

Reference: RIN # 3038-AD08
Docket: CFTC-2012-0037

Dear Mr. Pullen:

First, let me thank you for arranging yesterday's meeting. We found it very informative, and we hope you did as well.

I wanted to further address three items that came up during the meeting.

First, we noted the staff's concern about sparse data and its impact on block threshold calculations. We would envision two main reasons for sparse data: 1) persistent low trading volume lasting a year or more, and 2) a new product which, although it may be popular, has too short a history for reliable calculations. We would suggest that the rule establish a minimum number of transactions for the calculation to be run at all, and we suggest 250 as the minimum, which equates to approximately one transaction per day for seasoned products. We suggest that any product with fewer than 250 transactions have a block threshold of zero, making all trades in that instrument block trades.

The second item was the expressed concern that options products in particular could pass through liquidity cycles as the price of the underlying moves in relation to the option strike price. We note that such a sequence, as where the option moves from deep-out-of-the-money to at-the-money to deep-in-the-money, can have two impacts: on the option's volatility and on its liquidity. Since we understand that the block rule is focused on liquidity and not volatility, we think that the block calculation as we have proposed it will serve its purpose quite well in this instance. If deep-outs or deep-ins have low average trade sizes, their block thresholds will be appropriately low. If they become at-the-moneys and their average trade size rises, their block thresholds will rise appropriately. Thus we think the methodology will work as desired in this case.

The third question related to the possibility of traders moving transactions between product types in order to avail themselves of lower block thresholds. The example presented was of a trader using deep-in options as a substitute for a transaction in the underlying because the option threshold is lower than the underlying's. We note that the trader is taking on two risks in doing that. The first is that the liquidity of the option is presumably lower, which is why the block threshold is lower, so any large position established will be more difficult to hedge or unwind. The second is the the option is not a perfect substitute for the underlying, as its delta would fall if its intrinsic value fell. We also note that the

advantage gained by doing a block trade is very temporary, not permanent. Thus we don't think this instance will be economically attractive for dealers, and, if used, would not actually damage the Commission's oversight function.

We also noted the staff's concern about the use of UPI in our comment letter, since that implementation might be some time off. We believe that the suggested methodology can work on any classification schema used by the industry as a whole, and only used the UPI in our letter because we understand it to be the stated objective of the industry.

If we missed any of your concerns, please let us know. As always, we would be pleased to discuss this letter with the CFTC's commissioners or staff at your convenience, and would especially like to talk about how the methodology would actually be implemented when the time is right. We understand that this letter will become part of the public record.

Very truly yours,

George Bollenbacher
Head, Regulatory Reform Practice
george.bollenbacher@kinetixtt.com